M3 PROPERTY

SPECIALIST
INDEPENDENT
VALUATION

NATIONAL RESIDENTIAL DEVELOPMENT MARKET INSIGHT

JULY 2023

“SENTIMENT IS CAUTIOUS BUT NOT NEGATIVE ACROSS AUSTRALIA’S RESIDENTIAL DEVELOPMENT MARKETS”

- Luana Kenny
Managing Director VIC

There are multiple factors influencing Australia’s residential development market, and in a recent NAB Commercial Real Estate Property Development Webinar, I presented on some of these key issues and the way they are impacting markets. Specifically, I discussed Adelaide, Brisbane, Melbourne, Perth and Sydney markets in the presentation.

Claire Hains, Director, Victoria at M3 Property also provided her insights on the apartment and townhouse market in the presentation.

ARE WE IN THE PERFECT STORM?

The major issues and challenges we’re seeing across residential markets right now include:

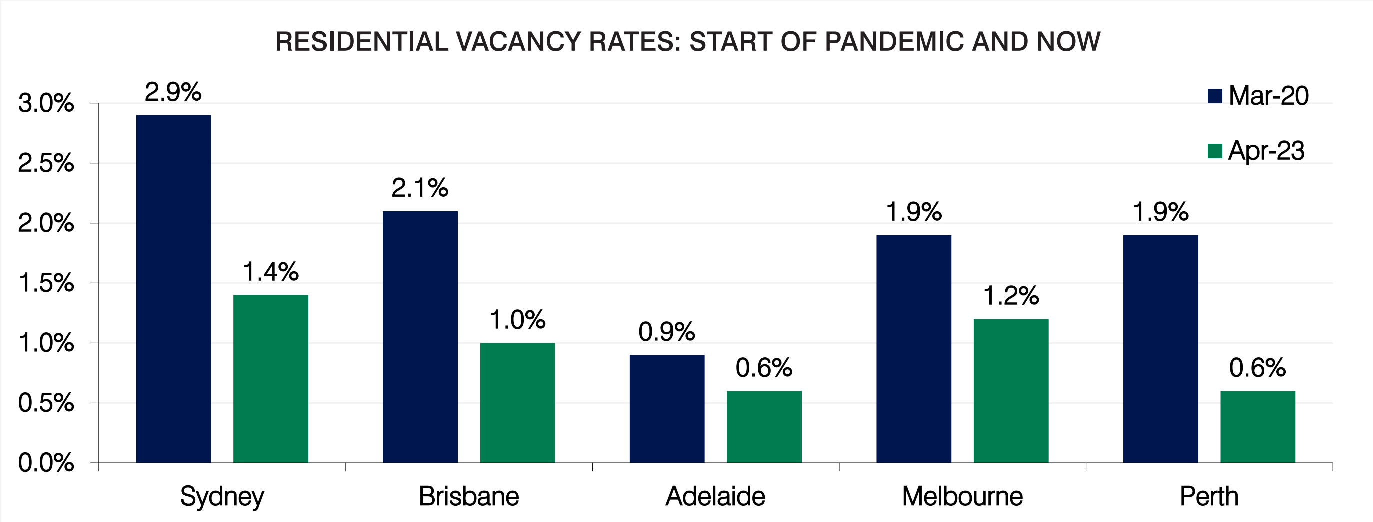
- Supply constraints
- Housing affordability
- The ability to deliver housing
- The rental market

There are a few consistent factors playing out in all markets. The top two issues we’re seeing are firstly supply, and secondly population growth.

SUPPLY AND DEMAND IN AUSTRALIA'S RENTAL MARKETS

Australia historically has seen record low interest rates which has led to growth over the last couple of years. However, as we've started to see interest rates increase, we've seen a slowdown in various markets to a certain degree.

Australia is in a rental crisis, highlighted by the low vacancy rates being seen compared with pre-COVID vacancy levels when they were on average nearly double what they are currently.



Source: SQM, M3 Property

MARKET RISK FACTORS TO LOOK OUT FOR

The biggest risk we see currently across several markets is planning risk. This is particularly true across NSW and Victoria, where there have been prolonged application periods which are constraining supply.

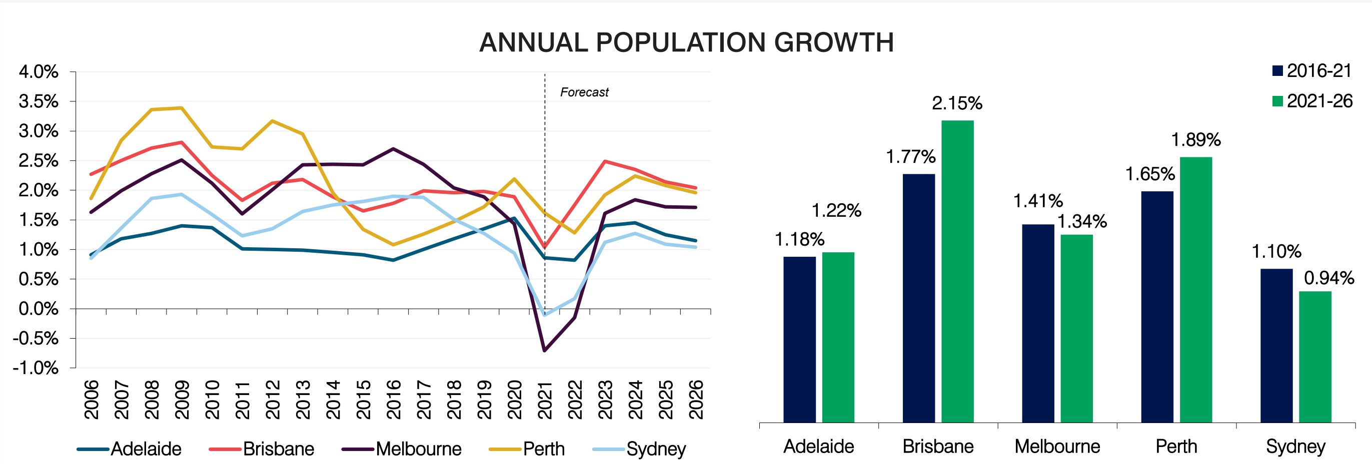
Construction and building industry insolvencies, combined with skilled labour shortages, have impacted supply and feasibilities in the valuation space.

POPULATION GROWTH

Australia is expecting significant population growth over the coming years.

Melbourne and Sydney have traditionally been the beneficiaries of population growth. However, during COVID, there was a significant exit from both these states, with Queensland and Perth the primary beneficiaries due to factors including lifestyle and affordability.

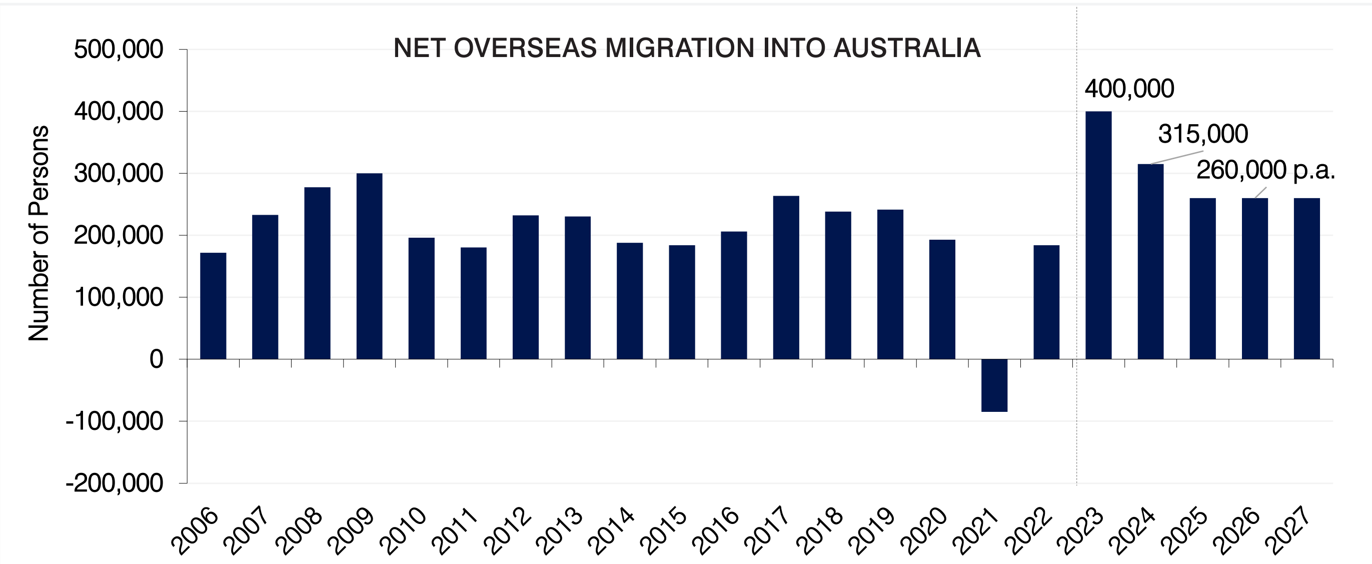
Melbourne and Sydney have both bounced back, although are not at pre-COVID levels but in 2024 are expecting an increase in interstate migration again.



Source: BIS Oxford Economics, M3 Property

Over the next five years, across Australia we are expecting Net Overseas Migration (NOM) to average 299,000 persons per annum or 1.5 million over the same period. This is in comparison to an average of circa 230,000 to 235,000 persons per annum during 'normal' times.

The key questions are: how are we going to house them, and how are we going to deliver that housing?



Source: ABS, Federal Budget Papers, M3 Property

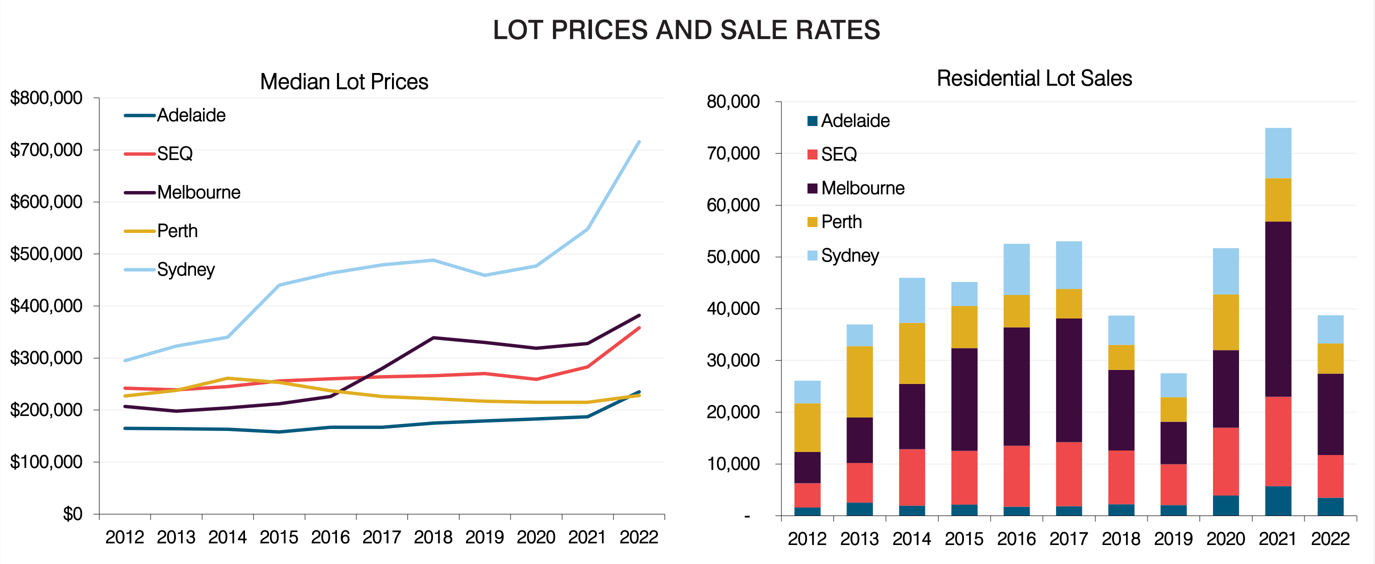
LOT PRICES AND SALE RATES FOR RESIDENTIAL ENGLOBO LAND

Particularly in NSW, there has been significant growth for lot prices in the englobo market, which is off the back of low supply.

Englobo land is land that is undeveloped or has minimal development; is largely unserviced; and zoned to allow for subdivision into smaller parcels.

The affordability issue in NSW is starting to have a real impact, and sales rates have come off significantly in both NSW and Victoria,.

NSW has generally had lower sale rates compared to Victoria, and they've generally trended around 4 to 5 lots per month per estate on average. In 2021, lot prices were particularly strong across all states and this is where significant growth was seen in lot pricing.



Source: UDIA, M3 Property

We saw a lot of pent-up demand come forward in 2021. As an example, Melbourne saw about 34,000 lots sold that year. Generally, the average lots sold in a year is in the order of 15,000 to 19,000 lots, so it was a significant increase from that traditionally seen, taking up a higher proportion of existing supply.

In 2023, Melbourne ticked into some oversupply which was short-lived.

Across the five states, approximately 40-45,000 lots are delivered per annum. In 2021, we saw about 75,000. This dropped to about 70,000 in 2022.

Population growth underpins all markets across the country. We have 1.5 million people coming into the country in the next five years, and we need to house them. The englobo market is not going to be able to keep up with that. We're going to have to see a bit more coming into the apartments and townouse market.

FORECAST OVER THE NEXT 12 MONTHS

In Sydney and Melbourne, we've seen a slowdown in lot pricing in 2023 which we expect will continue for the remainder of the year. However, we expect that to start to uptick into 2024 and we'll start to see some improvements in this market.

Going forward, one factor that M3 Property looks at when looking at affordability around growth areas is to look at the median house price.

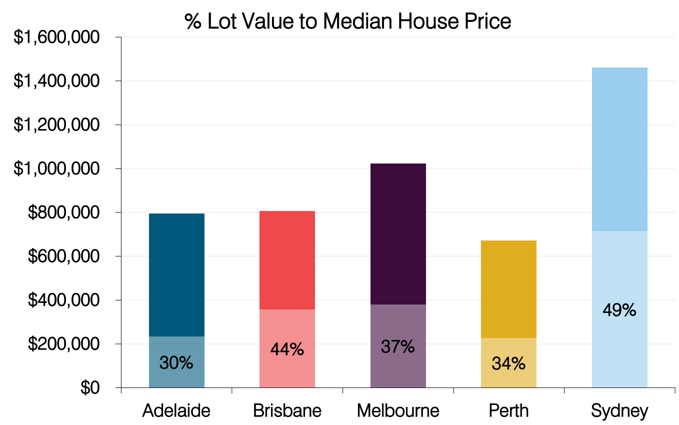
Generally around 30-35% of the land price against the median house price is where the market is affordable.

Brisbane is an interesting case because pricing has come up to about 44%. Brisbane saw significant growth in the South-East Queensland market, which has tipped it over to being less affordable which was a real driver of net interstate migration. This is a market we're watching in particular.

Adelaide, Melbourne and Perth are around the affordable mark, and they offer the most opportunities going forward.

MEDIAN LOT PRICE VS MEDIAN HOUSE PRICE

Capital City Market	Median Lot Price 2022CY	Median House Price March Qtr. 2023	% Lot Value to Median House Price
Adelaide	$235,000	$795,364	30%
Brisbane	$358,000^	$805,818	44%
Melbourne	$382,000	$1,023,116	37%
Perth	$228,000	$672,177	34%
Sydney	$716,000	$1,459,856	49%



Source: UDIA, Domain, M3 Property
Note: ^ South East Queensland

APARTMENTS AND TOWNHOUSES MARKET

Claire Hains, Director, Victoria at M3 Property also presented on the apartments and townhouse market across the same cities, Adelaide, Brisbane, Melbourne, Perth and Sydney.

Historically, the growth in unit prices across markets has increased at a relatively stable rate. In 2020 and 2021 for all states but Queensland, COVID brought forward pent-up demand off the back of a variety of factors including government incentives – particularly the home builder grant; low interest rate environment; low unemployment and higher levels of household savings.

The outlook for WA is relatively positive but it’s traditionally been its own market, while NSW has come off a period of large amounts of supply behind 2012 and 2017, and stabilised as demand was matching supply during that period.

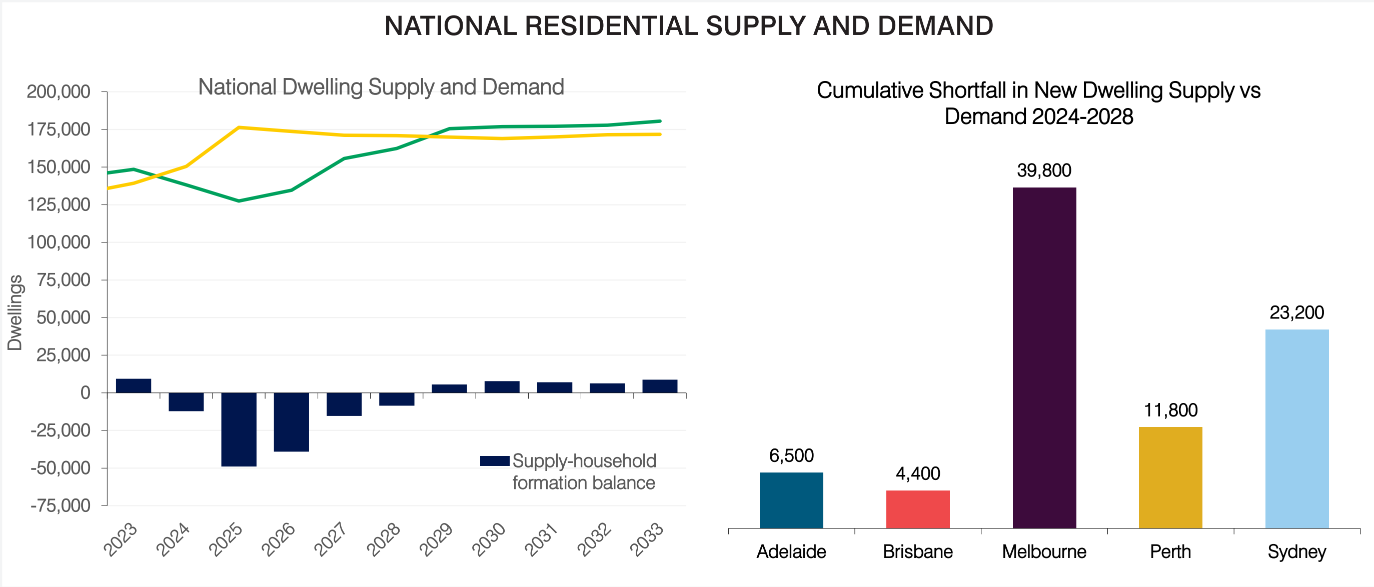
Adelaide is tracking relatively well and has seen a significant increase in the median house price over COVID which in turn is driving more demand for apartments and townhouses.

SUPPLY AND DEMAND MOVING FORWARD

Nationally, we’ve seen significant increases in interest rates, low population growth and historically high construction costs.

These factors have caused challenges for developers to build feasible projects and has meant that our levels of supply have been low across the country.

Couple this with the forecast increase in population growth to return over the next few years, and the increase in demand that brings, we’ve got a large shortfall in new dwelling creation which will continue until around 2028. This shortfall is leading to a significant increase in median rents nationally.



Source: NHFIC, M3 Property

Current rental growth we're seeing across the country is between 13-24%.

The increase in rents is strengthening the demand for sites from build-to-rent (BTR) operators. Their model is based upon holding whole apartment buildings for investment purposes.

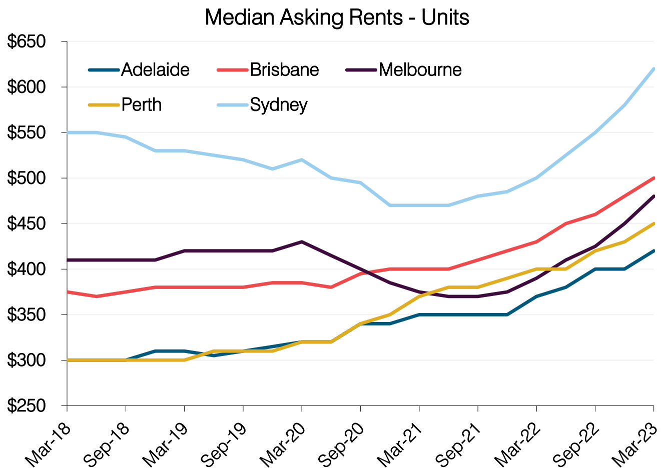
To date nationally, approximately 70 sites providing a total of 23,000 units have been purchased by BTR operators.

BTR provides a different housing experience to what's historically been seen in the Australian market. It will help to fill the void, but it's certainly not the solution to our housing shortages.

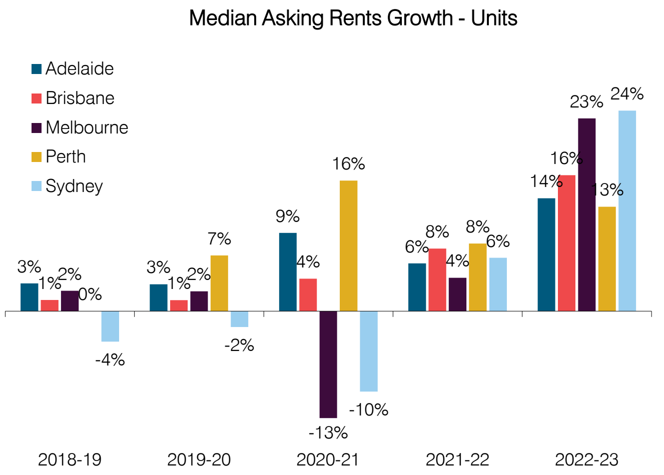
It's also not providing more supply into the market. It's purely replacing what would have been sold down to the market to individual purchasers, both owner-occupier and investment, to purely providing rental accommodation. If anything, it's contributing to less supply in the build to sell part of the market.

The flipside is that the lifestyles and demands of younger people are leaning towards longer-term renting being part of our culture moving forward, with the Australian dream of owning a home becoming not as important as it has been historically.

MEDIAN LOT PRICE VS MEDIAN HOUSE PRICE



Source: Domain, M3 Property



Source: Domain, M3 Property
Note: Growth is for y-o-y March quarters

AN INABILITY FOR FEASIBILITIES TO MEASURE UP

A big factor contributing to the shortage in supply to the market is the inability for feasibilities to stack up.

Some of the feasibility challenges being experienced by developers at the moment include:

1. Revenues are being squeezed thanks to the cost of living and increased interest rates.

2. It's harder for developers to achieve pre-sales, which leads to potential funding difficulties.

3. Development costs, and particularly construction costs, are not going to be getting back to pre-COVID levels.

4. There is opportunity for revenue growth, and we are forecasting revenue growth in all markets in 2024. One of the significant changes we need to see as an industry is planning reform – particularly in the bigger markets of NSW and Victoria.

We need to increase densities in areas that are already serviced by essential infrastructure, and we need to make that planning process more seamless.

To find out more about the national Residential market, contact info@m3property.com.au.

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